economic trends

March 2014

Alberta buoys Canada's labour market

After a strong finish to 2013, Alberta has entered 2014 with momentum. Alberta continues to lead the provinces in population growth and has accounted for the vast majority of the jobs created in Canada over the last 12 months. As reported in the Economic Outlook of Budget 2014, Alberta's economy is forecast to expand by 3.7% this year; the fifth straight year above the province's historic trend of around 3%.

Key Indicators			Seasonally adjusted unless otherwise indicated.
Indicator	**Latest Month**	**Value**	**Change year-over-year (y/y)**
Employment (thousands)	February	2,262	+3.8%
Unemployment Rate	February	4.3%	-0.2 p.p.
CPI Inflation	January	2.4%	+1.5 p.p.
Retail Sales	January	$6.4B	+9.8%
Housing Starts (annualized)	February	35,700	+3.9%
Rigs Drilling (unadjusted)	March	307	0.4%
Manufacturing Shipments	January	$6.5B	+7.0%
Exports (unadjusted)	January	$9.9B	+12.5%

Source: Statistics Canada, CAODC, CMHC. p.p.= percentage points.

Alberta Household Sector

National job gains concentrated in Alberta

Alberta continues to propel Canada's labour market. Over the past 12 months, Alberta has created 82,300 jobs, which represents 87% of all new jobs in Canada (Figure 1). Job growth has shifted to the goods sector following service-led growth in 2013. Growth in earnings has also picked up, hitting a 7-month high of 4.6% year-over-year (y/y) in December.

Consumer spending remains healthy

Retailers in Alberta are benefiting from strong job and earnings growth in the province. Retail sales growth has accelerated in every month since August, hitting a 2-year high of 9.8% y/y in January. While growth remains broad-based across retail categories, sales from vehicle dealers have been particularly strong.

Energy and shelter costs pickup

Inflation has held above 2% for the past three months. While energy prices continue to be a driver of inflation, shelter costs have also exerted pressure. Growth in owned accommodation costs has accelerated for the past five months, hitting 3.6% y/y in February, reflecting recent strength in Alberta's housing market.

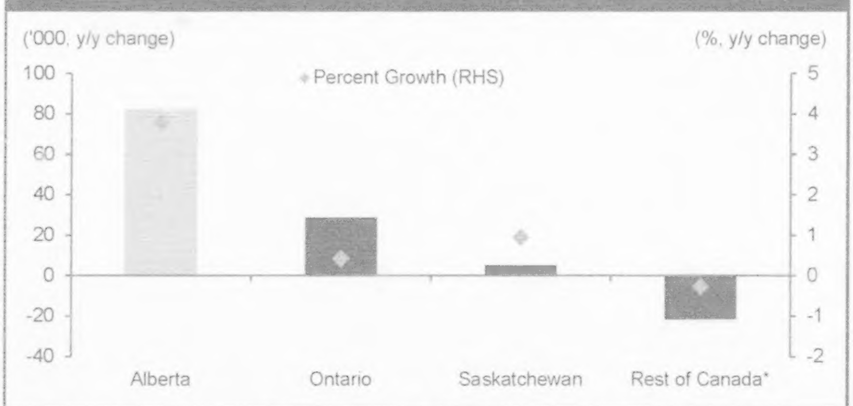
Alberta leads in population growth

Lured by job opportunities, people continue to move to Alberta. Alberta's population grew by 3.4% y/y as of January 1, 2014. This is the fifth straight quarter that growth has exceeded 3% growth. Alberta gained 134,300 people over this 12-month period, the highest increase among the provinces (Figure 2). Net international migration hit the highest fourth quarter level on record. While Alberta continued to add people from other provinces as well, net interprovincial migration moderated to a 9-quarter low.

Calgary's housing market takes off

Persistently strong population growth and flood reconstruction in southern Alberta has supported new home construction in the province. Housing starts have remained above 35,000 (seasonally adjusted at an annual rate) for the past five months. Calgary has driven recent gains, with the city's starts 54% higher in the first two months of 2014 compared with the same time last year. Strong housing demand in Calgary is also reflected in the number of unabsorbed new dwellings, which have tumbled to the lowest levels since late 2007. On the resale side, Calgary's market has been firmly in a seller's market since April

Figure 1. Employment Growth in February



Source: Statistics Canada *All remaining provinces had negative or zero employment growth.

2012, with a sales-to-new-listings ratio of 0.73. Since February 2013, Calgary has led the major Canadian cities with the strongest year-over-year price increases for new homes. After a strong increase in 2013, Edmonton's housing starts have drifted downward in recent months while new home prices have remained relatively flat.

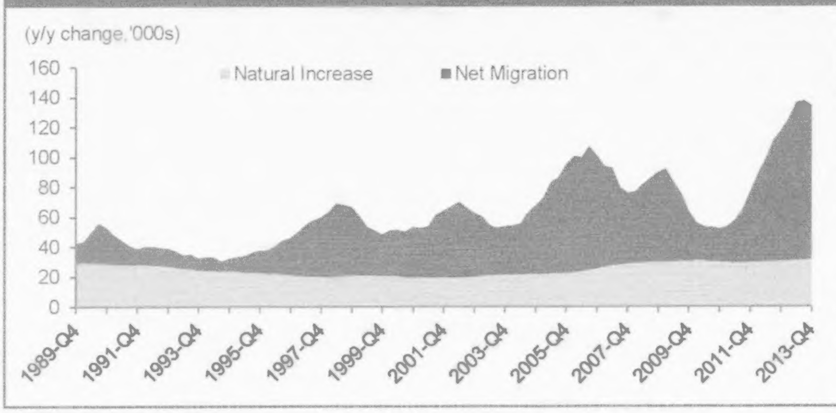
Alberta Business Sector

Oil and gas sector powers ahead
Output in Alberta's energy sector continues to strengthen. Year-over-year growth in energy exports has been in the double digits for the last five months to January, fueled by a combination of higher prices, rising production and a lower Canadian dollar. Another sign of strength is capacity utilization in Canada's oil and gas industry, which hit its highest rate in a decade at 86% in the final quarter of 2013.

While the vast majority of Alberta's energy mix is crude oil, natural gas exports have also trended higher. A brutally cold winter has led to storage drawdowns and higher prices of natural gas, pushing the value of exports higher and contributing to higher gas drilling activity.

Strong start for manufacturers
Alberta manufacturers have seen their sales trend upward trend since late 2012. Shipments started 2014 with a 7.0% y/y increase in January, with petroleum, chemical, and machinery products all recording double digit gains.

Figure 2. Alberta Population Growth



Source: Statistics Canada

More goods moving by rail
Western Canada rail volumes continue to trend higher, with carloadings up 4.7% in 2013. Reflecting constraints in the pipeline network, carloadings of crude petroleum and fuel oils have increased four-fold in the last decade, surging by 71.6% last year alone. Despite the gains, crude petroleum accounted for only 6% of rail carloadings in Western Canada last year (Figure 3).

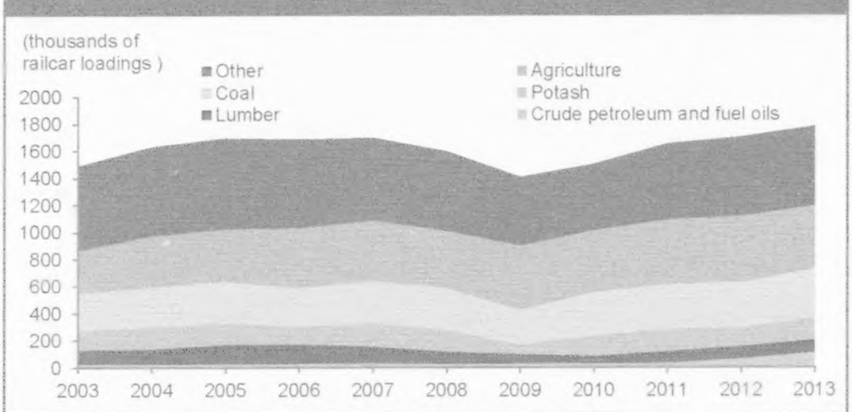
Global Economy

Canadian job growth cools
As of February, there were just 94,700 more jobs in Canada than in February 2013. This is the lowest annual increase since the recession and well below the historic average. What job creation there was took place mainly in Alberta, Ontario and Saskatchewan together adding 116,200 (Figure 1), while the remaining seven provinces had combined job losses of 21,500 over the last year. Weak job growth has not translated into weak real GDP growth as year-over-year GDP grew by 2.7% in the fourth quarter, the highest growth rate since 2011.

Conflict in Ukraine buoys oil prices
The conflict between Russia and the Ukraine is having ripple effects in financial and commodity markets. Russia is the third largest crude oil producer and second largest producer of natural gas, with the bulk of Russia's energy exports going to Europe. The possibility of sanctions has helped push WTI, the North American benchmark oil price, above US$100 /bbl.

Cold weather gives the economy chills
Most of North America has experienced one of the coldest winters on record. The severe winter weather has led to power outages, disrupted rail, air and highway transportation, and lowered sales at retail outlets. Cold weather has also pushed up energy prices, particularly for natural gas, which rose to a 5-year high in early March. The Federal Reserve and others have blamed cold weather for weak job growth in December, January and February, each of which posted job gains below the average for the previous 12 months.

Figure 3. Western Canada Rail Shipments



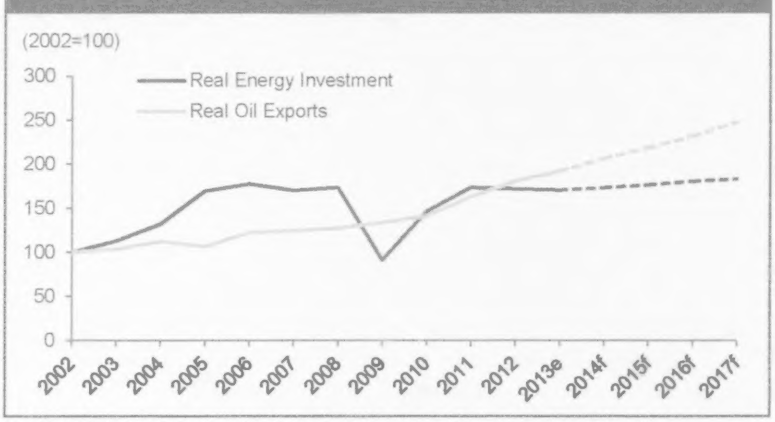
Source: Statistics Canada

Surging oil production lifts Alberta's economy

Alberta's oil and gas industry remains critical to the province's economic outlook. The industry accounts for nearly two-thirds of business investment, while energy products make up about three-quarters of the province's international goods exports. Investments in the oil sands are paying off, translating into large production gains and will drive the province's exports going forward. Oil sands gains will more than make up for dimmer prospects in the natural gas industry, where a glut of US shale gas has discouraged drilling for dry gas and kept prices at historically low levels, notwithstanding recent price gains caused by cold weather.

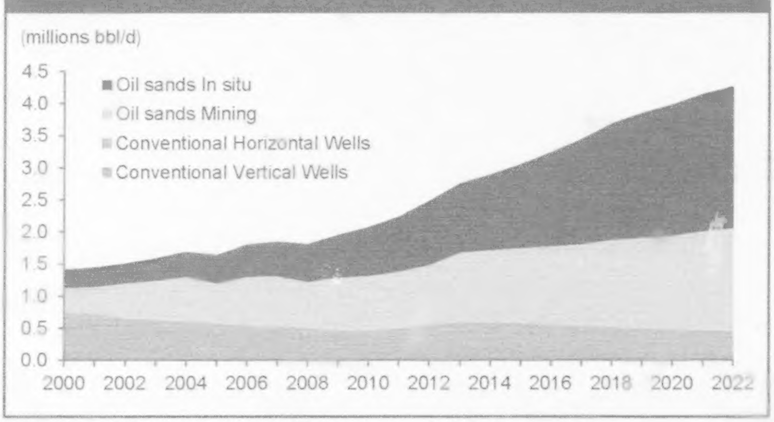
As reported in Budget 2014, prospects for the oil industry remain strong. An improving global economic outlook is supporting global oil prices, while the recent depreciation of the Canadian dollar has increased producer revenue. In addition, crude-by-rail has alleviated immediate pipeline transportation constraints,though uncertainty remains over market access due to delays in pipeline projects.

Figure 1. Alberta Real Energy Investment and Oil Exports



Source: Statistics Canada, Alberta Treasury Board and Finance - *Budget 2014*

Figure 2. Alberta Oil Production by Extraction Method



Source: Alberta Energy Regulator, ST-98.

Improved market conditions means that investment is expected to continue. In addition to new projects, such as the Fort Hills mine project, large numbers of existing projects will require investments in sustaining capital. Statistics Canada survey of investment intentions points to oil and gas investment of $55.2 billion in 2014, including $33.4 billion in the oil sands.

While energy investment will remain elevated, its growth will be far outpaced by oil exports, as a number of existing projects expand and new projects come on line (Figure 1).

Oil sands lead the way

Large scale investment in oil sands projects have increased production capacity, and paved the way for large increases in oil exports going forward. Over the last 10 years, nearly $180 billion has been invested in oil sands projects, overtaking conventional oil and gas as the highest source of investment in the province in 2011. A great deal of this investment has already yielded a return, with production more than doubling over the last decade to over 2 million barrels per day in 2013.

Mines are large scale projects, with higher initial investment and production compared with in situ projects, which use steam to extract oil beneath the earth's surface. It is estimated by the Alberta Energy Regulator that the mine supply costs (excluding upgrader) in 2012 ranged from approximately $US70-85 per barrel, compared with $US50-80 for in situ. Mine projects are typically much larger than a typical in situ project, with the average oil sands mine having capacity of over 100,000 barrels

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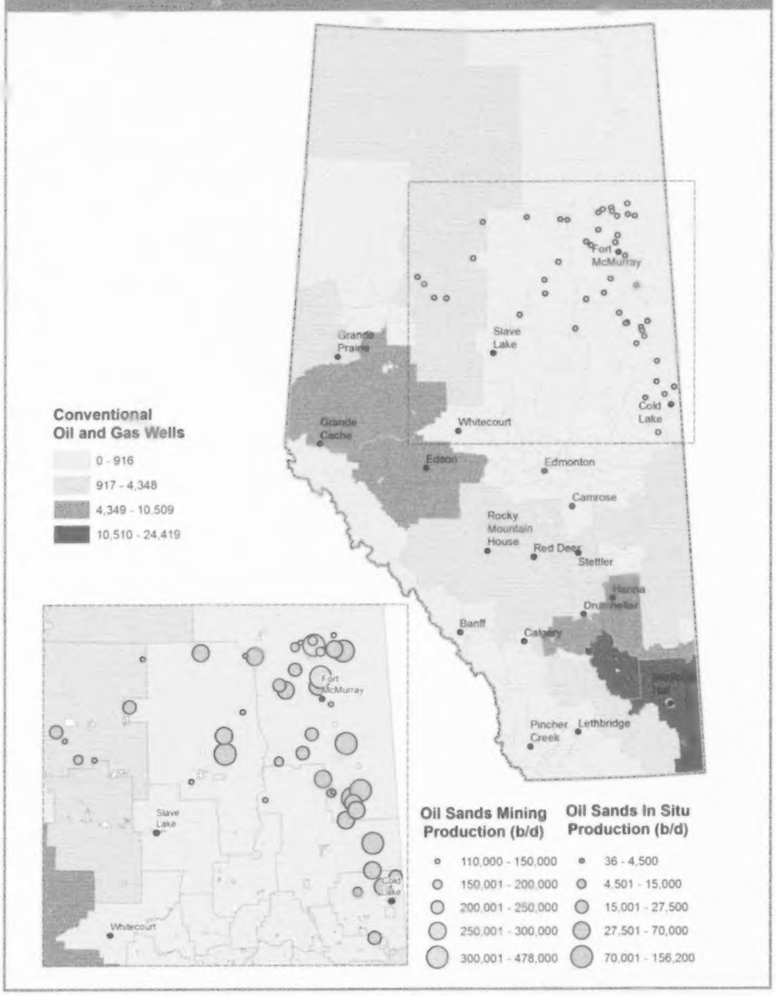
per day, compared with the average commercial in situ project producing 10,000-30,000 daily barrels per phase.

While mines result in higher production per project, the bulk of Alberta's reserves exist too far underground to access via mine extraction. Successful commercialization of in situ extraction, such as steam-assisted gravity drainage (SAGD), has increased the amount of recoverable reserves. As such, in situ will be the predominant extraction method moving further into the future. Currently in situ represents roughly half of total production, with its share expected to expand considerably (Figure 2).

Horizontal drilling supports conventional oil production

In Alberta's conventional oil industry, horizontal drilling and fracturing technologies have unlocked previously unrecoverable reserves. As a result, conventional oil production has risen in each of the last two years, reversing a 40-year downward trend. Total conventional oil production and investment are anticipated to hold around current levels, led by further expansions in horizontal well drilling. Conventional production could surprise to the upside if significant tight oil reserves, such as the Duvernay formation, become more prolific.

Figure 3. Alberta Oil and Gas Activity in 2013



Source: Alberta Energy and Alberta Treasury Board and Finance

Production centred in Wood Buffalo

Oil sands production is focused in an area that runs north of Fort McMurray and south to around Cold Lake (see Figure 3). Mines are located in relatively close proximity as only a small portion of oil sands deposits are mineable. In situ projects are generally smaller in initial production but many projects have the potential to be expanded to well over 100,000 barrels per day.

Conventional oil and gas activity is less concentrated. There were over 140,000 producing oil and gas wells in the province last year, of which 70% were natural gas. The highest concentration of wells in 2013 was in the southeast corner of the province. This area is largely comprised of natural gas drilling but also has oil activity. Another area of high well activity is in the central west part of the province where much of the province's drilling for conventional oil takes place. New horizontal drilling of the Montney and Duvernay formations could lead to more wells and production from the northwest corner of the province.

A strong outlook...with risks attached

The oil and gas industry is expected to remain a key driver of Alberta's economy, led by elevated investment and large increases in oil sands production. There are risks to this outlook. Without additional takeaway capacity from Alberta, the oil industry will continue to face large and volatile price discounts and rely more heavily on higher-cost rail transportation. Higher cost escalation, for example due to lower-than-expected inflows of new workers from outside Alberta, is also a risk. More globally, a slowdown in emerging markets, including the possibility of a financial crisis, would weigh on global oil prices and hurt growth prospects for Alberta's oil and gas industry. Renewed fiscal tensions in the Eurozone and the US could also weigh on global growth and oil prices. On the upside, an immediate alleviation of transportation bottlenecks and stronger-than-expected global growth could propel Alberta's oil and gas industry even higher.

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